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BEFORE THE ARIZONA CORPORATION COMI

FOR

JEFF HATCH-MILLER **CHAIRMAN** WILLIAM A. MUNDELL COMMISSIONER

MIKE GLEASON COMMISSIONER

KRISTIN K. MAYES COMMISSIONER

BARRY WONG COMMISSIONER 2006 AUG 21 A 10: 25

AZ CORP COMMISSION DOCUMENT CONTROL

Docket No. SW-02361A-05-0657

Arizona Corporation Commission DOCKETED

AUG 21 2006

DOCKETED BY N12

RUCO'S CLOSING BRIEF

INTRODUCTION

IN THE MATTER OF THE APPLICATION OF

BLACK MOUNTAIN SEWER COMPANY, AN

CORPORATION.

DETERMINATION OF THE FAIR VALUE OF

ITS UTILITY PLANT AND PROPERTY AND

FOR INCREASES IN ITS RATES AND CHARGES FOR UTILITY SERVICE BASED

The Residential Utility Consumer Office ("RUCO") submits this Brief in support of its position that the Arizona Corporation Commission ("Commission") should authorize a rate increase of \$5,470 for Black Mountain Sewer Company ("Black Mountain" or "Company"). RUCO recommends that the Commission not treat the Scottsdale Wastewater Treatment Capacity ("Scottsdale Capacity") as an operating lease given the change in circumstances that have occurred since the Company's last rate case. The Commission should treat the Scottsdale Capacity for ratemaking purposes as an asset and include it in the Company's rate base. RUCO further recommends that the Commission adopt its recommendations regarding the following:

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- Accumulated Deferred Income Taxes RUCO recommends the Commission decrease the Company's rate base by \$161,250 to include Black Mountain's allocated portion of Accumulated Deferred Income Taxes.
- Working Capital RUCO recommends that the Commission adopt its negative working capital allowance to reflect the fact that customers are required to prepay their sewer bill.
- 3) RUCO recommends the Commission adopt its adjustment to property tax expense based on the formula used by the Arizona Department of Revenue ("ADOR").
- Capitalized Expenses RUCO recommends that the Commission capitalize the Company's legal expenses associated with the operating agreement with the Town of Carefree and the expenses related to training on safety equipment.
- Sharper Sharpe

Finally, RUCO recommends the Commission adopt its positions on income tax expense and Cost of Capital.

THE COMMISSION SHOULD REJECT THE JOINT RECOMMENDATION OF STAFF AND THE COMPANY TO CONTINUE TO TREAT THE SCOTTSDALE CAPACITY AS AN OPERATING EXPENSE.

BACKGROUND

The issue of the Scottsdale Capacity dates back to the Company's last rate case, decided in two phases in 1995 and 1996. In that case, the Company's predecessor, Boulders Carefree Sewer Company ("Boulders") applied for, among other things, ratemaking treatment of the Scottsdale Capacity. Boulders purchased the capacity from the City of Scottsdale with the proceeds of a loan it obtained from its parent Company at the time – Boulders Joint Venture. RUCO 11 at 4.1 Boulders had originally entered into negotiations with the City of Scottsdale in 1989 and had not finalized an agreement prior to the filling of its previous rate case on January 6, 1995. Decision No. 59944 at 1-2. Since there was not a finalized agreement it was not possible for the Commission to incorporate the Scottsdale Capacity into a fair value finding until such time as the costs became known and measurable. Transcript at 369. The parties reached an agreement on the other aspects of the rate application and agreed to hold the docket open for the limited purpose of deciding the ratemaking treatment of the Scottsdale Capacity and the related financing. Transcript at 370. The Commission approved the settlement agreement. Decision No. 59166 (July 20, 1995).

Thereafter, Boulder and the City of Scottsdale finalized a capacity agreement and the capacity issue was brought back before the Commission. Id. The Company and RUCO both argued that the Scottsdale Capacity should be put into rate base and treated

¹ For ease of reference, trial exhibits will be identified similar to their identification in the Transcript of Proceedings. The Transcript volume number and page number will identify references to the Transcript.

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just like any other asset purchase. Id. Staff, however, took a very narrow view of the Commission's previous Decision (Decision No. 59166) holding the docket open and did not want to make a recommendation that would amend the Commission's previous fair value finding. Id. at 371-372. Despite the fact that the Company actually owned the capacity, Staff recommended that the capacity be treated as an operating lease because doing so had the effect of isolating the capacity issue from any other issue, including the Commission's previous fair value finding. Id. The Commission adopted Staff's illusory "operating lease" recommendation noting that Staff's recommendation "most nearly complies with the procedure outlined in the Settlement Agreement to govern this phase of the case." Decision No. 59944 at 6. Calling the loan an "operating lease" in the Company's last rate case was merely an expedient mechanism to incorporate the capacity into rates without amending the Company's fair value rate base.

In March 2001, Algonquin Water Resources of America, Inc. ("Algonquin") purchased the stock of Boulders. RUCO-11 at 4. The purchase was financed with equity from Algonquin and debt from Black Mountain to Algonquin (promissory notes). Id. The debt and equity are the capitalization that supports all of the assets of what is now Black Mountain Sewer Company, including the Scottsdale Capacity. Id.

THE COMPANY DOES NOT HAVE AN OPERATING LEASE WITH THE CITY OF SCOTTSDALE, AND FOR ACOUNTING PURPOSES, THE CAPACITY SHOULD NOT BE TREATED AS AN OPERATING LEASE

No party has argued or even suggested that the Company had, or currently has, an operating lease with the City of Scottsdale for the wastewater treatment capacity. The Company's predecessor, Boulders, purchased the capacity with the proceeds of a loan

from its parent company at the time. Id. Boulders no longer exists, nor does the loan the parent company made to Boulders exist. Id.

The circumstances have changed since the last rate case and the nexus connecting the capacity to an "operating lease" is even farther removed. The loan no longer exists between Boulders and its parent. The combination of debt and equity utilized to purchase the present company has not been, nor can it be, apportioned specifically to the treatment capacity. The Company now has an asset on its balance sheet supported by a combination of debt and equity which cannot be specifically apportioned to the treatment capacity. The Commission should recognize the change in circumstances and treat the capacity as an asset for ratemaking purposes.

It has been suggested that if RUCO disagreed with the Commission's prior order regarding the capacity (Decision No. 59944) RUCO's remedy was through the appellate process. Transcript at 373. The issue is not whether the operating lease treatment was appropriate in 1996, but whether it remains appropriate today in light of the unusual procedural posture of the issue in 1996, and the vastly changed circumstances. In 1996, the Commission approved the operating lease methodology because it found that that approach most closely complied with the procedural requirements set forth in the Commission's Decision in the first phase of the proceeding in 1995.

It is perfectly appropriate for the Commission to revise a previously adopted ratemaking treatment when circumstances have changed. For example, the Commission removes plant from rate base if it is no longer used to provide utility service, even if the utility continues to own the plant. Here, the circumstances that were the foundation of the "operating lease" treatment – the desire to not amend the fair value finding of Decision 59166, and the specifically-identifiable loan from the Boulders' parent to finance the

capacity acquisition – have vanished. Thus, it is appropriate to treat the Scottsdale Capacity as an asset and include it in the Company's rate base.

THE COMPANY IS NOT PREJUDICED BY CHANGING THE RATEMAKING TREATMENT OF THE SCOTTSDALE CAPACITY

Should the Commission apply the proper ratemaking treatment and treat the capacity as an asset, the Company will still be able to recover the cost of the Scottsdale Capacity. The purchased treatment capacity will be treated as a utility asset and included in rate base, which will allow the Company to earn the Commission-approved rate of return on it. RUCO -13 at 9. Through RUCO's recommended level of depreciation and amortization expense, the Company will fully recover the principal portion of the loan and will have the opportunity to recover the interest associated with the loan as a below-the-line expense that will reduce the Company's income tax liability. Id. Moreover, if the capacity is rate based, there would be no need for the Company consultant's gross-up adjustment on the principal portion of the loans since the loans, and the asset (i.e. Scottsdale treatment capacity) that were purchased by the Company will be treated as they would under normal ratemaking practice. Id. The Company would not be prejudiced by now affording the proper rate base treatment of the Scottsdale Capacity.

Commission ratemaking determinations are always subject to revisions in a subsequent rate case. The Commission never indicated or suggested in Decision No. 59944 that its 1996 Decision regarding the Scottsdale Capacity was the appropriate ratemaking treatment of the Scottsdale Capacity for all time. It is clear that the Commission's 1996 Decision recognized the circumstances at the time and resolved that

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extra-ordinary ratemaking treatment was necessary under the circumstances that existed then and not now.

It has been suggested that it would be unfair to the Company to now change the accounting treatment because the Company lost out on rate base treatment on the front end. Transcript at 376-377. The unfairness, however, would be to the ratepayers if the Commission were to continue to apply the same accounting treatment, for several reasons. First, when Algonquin purchased the stock of Boulders it had no basis to believe that the Commission would be forever bound to the accounting treatment it approved in Decision No. 59944. The Company did not assume it was forever bound by the rates the Commission approved in the Company's last rate case, so it should not expect the Commission would be bound by its Decision regarding the non-existent operating lease. Every Company knows that there is risk in filing a rate case. The Commission could reject its request or even lower its rates. Everything, unless stated otherwise by the Commission, is subject to change depending on the circumstances. The Company's circumstances have changed and the Commission should set rates that reflect the changed circumstances.

Second, the Company does not have an "operating lease" with the City of Scottsdale. From a regulatory accounting perspective the capacity is an asset, and not an operating lease. It does not make sense to continue to treat the capacity as something other than what it is because 10 years ago the Commission did not want to amend a fair value finding and felt procedurally restricted to consider the capacity as an operating lease. Moreover, it is bad policy, and has never been the policy of the Commission to blindly and recklessly adhere to its previous Decision and ignore current and changed circumstances. RUCO-12 at 3.

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BACKGROUND

and Staff's recommendation.

DEFERRED INCOME TAX ADJUSTMENT

In its application, the Company's proposed rate base reflected a zero balance for ADIT. RUCO-11 at 10. With few exceptions, RUCO is not aware of any Arizona utility filing a rate application that has proposed a rate base with no ADIT. RUCO, in a data request, asked the Company about it and was advised that the Company filed a consolidated tax return with its parent Company – Algonquin - and the ADIT balance resided on Algonquin's balance sheet. Id.

Finally, the continued treatment of the capacity as an "operating lease" deprives

ratepayers of the credit for that portion of the capacity for which ratepayers have already

paid. RUCO-11 at 7. While ratepayers are paying for 5% of this plant capacity each year

through "operating lease" expense, the "operating lease" methodology never provides

credit for the portion of the capacity that ratepayers have already paid for. When the

correct ratemaking methodology is used to account for this capacity, that credit is reflected

in the Accumulated Depreciation balance that serves to decrease rate base and, in turn,

decrease rates. The "operating lease" methodology robs ratepayers of this credit. Id.

THE COMMISSION SHOULD ADOPT RUCO'S RECOMMENDED ACCUMULATED

The Company has adopted Staff's Accumulated Deferred Income Tax ("ADIT").

Staff's recommendation was based on its misplaced reliance on unsubstantiated figures

provided by the Company. The Company's figures result in a tax asset, where customarily

ADIT is liability on a utility's balance sheet. The Commission should reject the Company

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 The majority of Arizona's larger utilities and many of its smaller utilities have parent company structures and file consolidated tax returns. Id. The practice of filing consolidated tax returns is common in the industry and these utilities apportion their percentage of their ADIT in their rate base. Id. And for at least five of Arizona's larger utilities that have parent company structures, their recent rate applications indicate an ADIT liability. Transcript at 102-106.

RUCO referred to the parent Company's <u>audited</u> 2004 annual report and identified the consolidated ADIT balance for the parent company as a whole. RUCO-11 at 11. RUCO then allocated a portion back to the Company based on the ratio of the purchase price of the Company to the parent company's total assets. Id. The result is RUCO's recommendation of a \$161,250 ADIT liability (i.e. reduction in rate base) Id. at 12.

Staff followed up on RUCO's ADIT inquiry and received information back from the Company indicating a \$164,000 ADIT asset. S-9 at 21. Staff relied on the Company's figures and recommended a \$164,000 rate base increase as its ADIT adjustment. Id. The Company, in its rebuttal testimony changed its position and joined in Staff's recommendation. A-2 at 9-10.

THERE IS NO BASIS TO SUPPORT THE COMPANY AND STAFF'S ADIT RECOMMENDATION

The Company's change of position late in this proceeding is at best, highly suspect. The Company, a sophisticated sewer utility, claims that it overlooked an ADIT adjustment that would have increased its rate base by \$164,000 in its original filing - a clear benefit to the Company. Then, after the Company realizes its oversight and has reviewed Staff's reasons for including the ADIT asset, the Company changes its position and concurs with Staff. A-2 at 9-10. Staff, however, has provided no reason for its recommendation other

than it relied on the Company's representation that its ADIT balance netted out to a \$164,000 asset. S-9 at 20-21. There is nothing on the books or in the Company's records provided to the parties that support the Company's figures. Transcript at 387. Moreover, the Company readily admits that nowhere on its 2002, 2003 and 2004 financial statements is there an entry for an ADIT asset. Transcript at 261. There is no basis to support Staff and the Company's recommendation and it should be rejected by the Commission.

It is not coincidence that utilities almost always report an ADIT liability. Simply stated, ADIT is just what its name implies – a deferred tax. The Company still owes the tax, it does not go away – it is still a liability. Transcript at 109 – 110. RUCO relied on the Company's representation that the Company's ADIT balance resided on its parent's consolidated return. RUCO then reviewed the parents ADIT balance, noted that it was a liability as is usually the case, and apportioned it accordingly. RUCO's methodology is the custom in the industry and is the best and most reasonable methodology for determining the Company's ADIT adjustment. The Commission should adopt RUCO's recommended ADIT adjustment of (\$161,250).

WORKING CAPITAL

A company's working capital requirement represents the amount of cash the company must have on hand to cover any differences in the time period between when revenues are received and expenses must be paid. Transcript at 386. The most accurate way to measure the working capital requirement is via a lead/lag study. The lead/lag study measures the actual lead and lag days attributable to the individual revenues and expenses.

The Company originally computed its cash working capital requirement using the formula method. The formula method assumes that there is an average lag of 45 days from operating maintenance and expenses, and an average lag of 15 days for purchased power expenses. RUCO-11 at 12. The formula method always generates a positive working capital allowance and does not consider the revenue leads and/or lags. Id., Transcript at 426. The formula method is not the best measure of working capital since it only can result in a positive working capital allowance even when a Company's working capital allowance is actually negative such as in the subject case. RUCO-11 at 12.

In its rebuttal testimony, the Company joined in Staff's recommendation of a zero cash working capital allowance. A-2 at 11. Staff's recommendation appears to be more of a policy consideration and not based on any analysis. Transcript at 433. Interestingly, Staff notes twice that when considering cash working capital it is inequitable to ignore a major component of the working capital analysis and selectively recognize other components. S-9 at 22 and 24. Staff's recommendation fails to follow its own admonishment on selective recognition of working capital components, since to arrive at a zero working capital recommendation necessarily ignores revenue lead days generated by the ratepayer's prepayment for services. It is undisputed that the Company, unlike many utilities, bills for service prior to fully rendering the service. RUCO-11 at 13. The due date, when compared to the mid-point of the service period, produces a revenue lag of approximately seven or eight days. Id.

Typically, as Staff has admitted in other Class A water utility cases, most utilities have a negative cash working capital requirement. Transcript at 386, See also the Direct Testimony of Staff's witness James J. Dorf at page 6 in Docket No. W-01303A-05-0405 Arizona American, Paradise Valley Water District Rate Application – "Staff has typically

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found that most sophisticated utilities will have a negative rather than a positive Cash Working Capital Allowance." The reason why a utility's working capital requirement is more likely to be negative is because the revenue lags are less than the expense lags. Transcript at 386. The likelihood of a negative cash working capital allowance is even more pronounced in this case given the Company's policy of billing customers before fully rendering service. Id.

RUCO's analysis, unlike the Company's and Staff's, considers both the revenue and expense lead and lags and results in a negative working capital allowance of \$87,253. RUCO-11 at 14. Moreover, RUCO's analysis shows that, at the very least, the Company's working capital allowance is negative. RUCO did conduct a lead lag study that used inputs from the Company's formula method for expense lags. Transcript at 429. RUCO calculated the revenue lead days based on actual customer bills showing the service period, bill date, and payment due date. RUCO 12 at 8. RUCO, to eliminate contention, accepted the Company's use of 45 lag days for expenses and 15 lag days for purchased power in its original recommendation using the formula method. Id. The Company's suggestion that RUCO's expense and purchased power lag inputs are now inappropriate is misplaced, makes no sense since the Company recommended the same lags when it was recommending the formula method, and should be disregarded. Transcript at 430.

To arrive at a zero or positive working capital recommendation, the study would have had to use an expense lag of 7.83 days or less. Transcript at 431. Given the lag associated with income tax (52 days), property tax (usually 211 days) and interest expense (usually 188 days) there is simply no way the Company has an expense lag of 7.83 days or less. Id. Staff and the Company's recommendation of a zero working capital allowance

ignore the expense and revenue components of cash working capital and should be rejected by the Commission.

CAPITALIZED EQUIPMENT

RUCO recommends that the Commission capitalize the expenses related to training on safety equipment and the Company's legal expenses associated with the operating agreement with the Town of Carefree. The cost for training people on the new safety equipment is a cost of putting those assets in place. Under GAAP accounting, those costs are required to be capitalized along with the safety equipment. The legal fees associated with franchises and operating agreements with state and local government entities are required under the Uniform System of Accounts to be capitalized in account 352 - Franchises. RUCO recommends capitalization of these two expenses. RUCO-12 at 9.

PROPERTY TAX

RUCO recommends the Commission adopt its adjustment to property tax expense based on the formula used by the Arizona Department of Revenue ("ADOR"). The evidence continues to show, despite the Commission's failure to recognize it, that the use of the ADOR formula to estimate property taxes is a much more accurate estimate of actual property tax than the methodology that the Company proposes and the Commission has historically adopted. This case is no exception. Ruco-13 17. RUCO's recommended property tax expense calculation was based on the ADOR property tax formula. Id. at 13. The property tax formula, as prescribed in ADOR's memo dated January 3, 2001, values water utilities, for property tax purposes by multiplying the average of the water utility's three previous years of reported gross revenues by a factor of two. Id. at 14.

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The Company has disregarded the revenues required under the ADOR directive and substituted in its place the adjusted test-year revenues twice and its proposed level of revenues once ("Company methodology"). Id. RUCO, for valuation purposes, has included the test year (2004) and the prior two years (2002, 2003) as directed by ADOR ("ADOR methodology"). Since the ADOR issued its memo, enough time has passed so that actual property tax figures for 2005 are available and the Commission can compare those figures to the estimated figures derived using the Company's and the ADOR methodologies. The Company's actual 2005 test-year property taxes were \$31,949. Id. at 15. Using the ADOR methodology, RUCO's estimated 2005 property tax assessment is \$35,410, a difference from the actual expense of \$3,461. Id. However, using the Company's methodology results in an estimate of \$45,745, a difference of \$13,796 from the actual expense. Id. This evidence clearly demonstrates that once again, ADOR's method more closely approximates the Company's actual post-test year property tax bill than does the Company and Staff methodology. The Commission should adopt RUCO's approach and recognize the ADOR methodology as the best measure of actual property tax expense.

The Company mistakenly claims that the ADOR methodology using historical inputs ignores the Company's proposed revenues. A-2 at 37. In fact, the ADOR formula using historical inputs accounts for additional revenues. The application of proposed revenues, however, to the ADOR formula is likely to overstate property tax expense because of the timing lags inherent in the accrual and collection of property taxes. The impact of additional revenues on property tax is not the same as the impact of additional revenues on income taxes. Whereas the effect of additional revenues on income tax is immediate, the effect of additional revenues on property taxes is not immediate because property taxes based on the increased revenues are not paid until more than a year after

new rates go into effect. Even then the increased revenues' impact on property taxes is tempered by the use of two earlier years' revenues. The full impact of increased revenues on property taxes will not be felt until four years after new rates go into effect. An understanding of this timing difference is critical to understand why the ADOR formula using historical inputs is a more accurate method to estimate property taxes than the use of adjusted and pro-forma revenues. This also explains why the new rates that will go into effect will not affect property taxes immediately. In RUCO's experience, the Commission has not gone more than one year beyond the test year to look at any other expense on the income statement. Here, the test year was 2004, and one year beyond that is 2005. RUCO established a level of property tax for 2005.

The Company and Staff recommend the Commission look beyond one year from the test year and consider new rates to estimate property tax expenses more than one year into the future. Historically, the Commission does not consider a post-test-year expense beyond one year because, among other things, it violates the matching principle and the used and useful principle. The ADOR formula using historical inputs, as RUCO has stated many times before, is forward looking and does consider the fact that new rates will be set. The Commission should adopt the ADOR formula using historical inputs.

The Company relies on previous Commission Decisions that conclude that RUCO's methodology, and hence the ADOR methodology, unreasonably understates property tax expense. A-2 at 37-38. With all due respect, the evidence has shown and continues to show, as in this case, that the ADOR methodology is the most accurate. In this case, had the Commission previously approved the Company's methodology, property taxes for 2005 would have been overstated by \$13,796 which would have allowed the Company to over

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earn for several years until that level of tax was actually assessed. The Commission should adopt the ADOR methodology.

INCOME TAX EXPENSE

RUCO recommends the Commission use the synchronized interest method for calculating the level of interest expense to be deducted from income taxes. The total reduction using the interest method is (\$31,808). RUCO-13 at 17, Schedule WAR-8

RATE DESIGN

RUCO recommends the Commission adopt the Company's current rate design with adjustments to the monthly charges in order to generate RUCO's recommended level of revenue.

COST OF CAPITAL

RUCO's cost of capital recommendations are based on two different capital structures. Should the Commission adopt the Company's pro forma Scottsdale Capacity position, RUCO is recommending a capital structure of 43 percent debt and 57 percent equity, which results in an 8.92 percent weighted cost of capital. RUCO-14 at 9. Should the Commission reject the Company's pro forma Scottsdale Capacity position, RUCO is recommending a capital structure comprised of 44 percent debt and 56 percent equity and a 9.45 percent weighted cost of capital. Id.

The Company is recommending a capital structure of 100% equity. Transcript at 132. Given the lack of any debt in its capital structure, it should follow that the Company's cost of equity would be low because of the decreased financial risk associated with no

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debt. Incredibly, the Company's cost of equity recommendation is 11.00% compared to RUCO's recommended 9.49% and Staff's recommendation of 9.60%. RUCO-14 at 10. The Company's cost of capital recommendation does not make sense and should be rejected by the Commission.

To the extent the Company has a response, it infers that it has risk associated with the debt service on the operating lease. The Company claims that there is no guaranteed recovery on the debt service. A-2 at 76. The Company's argument is simply wrong. If the Commission adopts the Company's pro forma operating lease expense figure, the Company will recover the inter-company loans on a dollar-for-dollar basis. RUCO 15 at 11. Therefore, there exists no financial risk associated with the inter-company loan. Id.

This lack of risk is the reason why RUCO is recommending two capital structures.

Id. Both capital structures, to be fair, bring the Company's capital structure and weighted cost of capital in line with the weighted capital structures and weighted costs of capital of the utilities RUCO used in its water company sample.

In terms of risk, RUCO's recommended 9.49 percent cost of equity, if anything, is generous. The water companies used in RUCO's analysis would be considered as having a higher level of risk than the Company because of their higher level of debt as compared to the Company. RUCO-14 at 52. Therefore, applying the 9.49% cost of equity derived from RUCO's DCF analysis to the Company is certainly fair and generous. By comparison, Staff has recommended a negative 30 basis point adjustment to reflect the Company's lack of financial risk in its cost of equity analysis. RUCO-15 at 16. RUCO's cost of capital recommendation is well reasoned, reasonable, fair, and should be adopted by the Commission.

CONCLUSION

RUCO recommends that the Commission not treat the Scottsdale Capacity as an operating lease given the change in circumstances that have occurred since the Company's last rate case. The Commission should treat the Scottsdale Capacity for ratemaking purposes as an asset and include it in the Company's rate base. RUCO further recommends that the Commission adopt its recommendations regarding the following:

- 1) Accumulated Deferred Income Taxes RUCO recommends the Commission decrease the Company's rate base by \$161,250 to include Black Mountain's allocated portion of Accumulated Deferred Income Taxes.
- 2) Working Capital RUCO recommends that the Commission adopt its negative working capital allowance to reflect the revenue leads that result from the prepayment of customer's sewer bills.
- 3) RUCO recommends the Commission adopt its adjustment to property tax expense based on the formula and inputs used by the ADOR.
- 4) Capitalized Expenses RUCO recommends that the Commission capitalize the Company's legal expenses associated with the operating agreement with the Town of Carefree and the expenses related to training on safety equipment.
- 5) Rate Design RUCO recommends the Commission adopt the Company's current rate design with adjustments to the monthly charges in order to generate RUCO's recommended level of revenue.
- 6) RUCO recommends the Commission adopt its reduction to income tax expense of (\$31,808).

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Finally, RUCO recommends the Commission adopt its 9.45% weighted average cost of capital if it adopts the Company's pro forma Scottsdale Capacity position and 8.92% if the Commission rejects the Company's pro forma Scottsdale Capacity.

RESPECTFULLY SUBMITTED this 21st day of August 2006.

Daniel Pozefsky Attorney

AN ORIGINAL AND THIRTEEN COPIES of the foregoing filed this 21st day of August 2006 with:

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